

AVATAR, INC.

FINANCIAL STATEMENTS

with

Independent Auditors' Report

Years Ended June 30, 2005 and 2004

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CARVER HOVEY & FLOREK, LLC

CERTIFIED PUBLIC ACCOUNTANTS

STEVEN L. CARVER, CPA
KATHLEEN L. HOVEY, CPA
BRENT R. FLOREK, CPA

INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
Avatar, Inc.
Ogden, Utah

We have audited the accompanying statements of financial position of Avatar, Inc. (a non-profit organization) as of June 30, 2005 and 2004, and the related statements of activities, functional expenses, and cash flows for the years then ended. These financial statements are the responsibility of the Organization's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Avatar, Inc. as of June 30, 2005 and 2004, and the changes in its net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated October 14, 2005 on our consideration of Avatar, Inc.'s internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grants for the year ended June 30, 2005. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

Carver Hovey & Florek, LLC

October 14, 2005

AVATAR, INC.
STATEMENTS OF FINANCIAL POSITION
June 30, 2005 and 2004

	<u>2005</u>	<u>2004</u>
ASSETS		
Current assets:		
Cash and cash equivalents	\$ -	\$ 31,858
Assets limited as to use (notes 1 and 2)	9,854	11,658
Accounts receivable	<u>222,942</u>	<u>182,640</u>
Total current assets	232,796	226,156
Property and equipment (net) (note 3)	707,675	687,443
Assets limited as to use (notes 1 and 2)	25,000	25,000
Deposits	1,950	1,950
Prepaid expenses	19,270	8,432
Intangible assets (net) (note 4)	<u>16,772</u>	<u>17,886</u>
	<u><u>\$ 1,003,463</u></u>	<u><u>\$ 966,867</u></u>
 LIABILITIES AND NET ASSETS		
Current liabilities:		
Checks drawn in excess of cash	\$ 5,255	\$ -
Accounts payable	62,848	63,360
Accrued interest	3,910	3,514
Accrued expenses	136,574	113,908
Officer loan payable (note 8)	20,631	-
Current maturities of long-term debt (note 5)	<u>26,385</u>	<u>25,217</u>
Total current liabilities	255,603	205,999
Long-term debt, less current maturities (note 5)	590,756	617,687
Net assets:		
Unrestricted	122,250	106,523
Temporarily restricted	<u>34,854</u>	<u>36,658</u>
	<u>157,104</u>	<u>143,181</u>
	<u><u>\$ 1,003,463</u></u>	<u><u>\$ 966,867</u></u>

See accompanying notes and accountants' report

AVATAR, INC.
STATEMENTS OF ACTIVITIES
Years Ended June 30, 2005 and 2004

	<u>2005</u>	<u>2004</u>
UNRESTRICTED NET ASSETS		
Unrestricted revenues:		
Public support contracts	\$ 2,426,823	\$ 2,393,861
Client fees and other	158,724	157,864
Net assets released from restrictions:		
Restrictions satisfied by payments	<u>25,004</u>	<u>25,251</u>
Total unrestricted public support and revenue	2,610,551	2,576,976
Expenses:		
Group homes	1,953,703	1,756,039
Family support	173,256	226,009
Supported employment	92,382	75,765
Management and general	<u>352,283</u>	<u>583,964</u>
Total expenses	2,571,624	2,641,777
Net assets reclassified as temporarily restricted	<u>23,200</u>	<u>25,208</u>
Total expenses and restrictions	<u>2,594,824</u>	<u>2,666,985</u>
Increase (decrease) in unrestricted net assets	15,727	(90,009)
TEMPORARILY RESTRICTED NET ASSETS		
Net assets reclassified as temporarily restricted	23,200	25,208
Net assets released from restrictions	<u>25,004</u>	<u>25,251</u>
Decrease in temporarily restricted assets	<u>(1,804)</u>	<u>(43)</u>
INCREASE (DECREASE) IN NET ASSETS	13,923	(90,052)
NET ASSETS AT BEGINNING OF YEAR	<u>143,181</u>	<u>233,233</u>
NET ASSETS AT END OF YEAR	<u><u>\$ 157,104</u></u>	<u><u>\$ 143,181</u></u>

See accompanying notes and accountants' report

AVATAR, INC.
STATEMENT OF FUNCTIONAL EXPENSES
Year ended June 30, 2005

	Group Homes	Family Support	Supported Employment	Management and General	Company Total
Salaries and related expenses:					
Salaries	\$ 1,357,420	\$ 149,527	\$ 71,532	\$ 176,523	\$ 1,755,002
Payroll taxes	105,680	7,162	5,560	27,956	146,358
	<u>1,463,100</u>	<u>156,689</u>	<u>77,092</u>	<u>204,479</u>	<u>1,901,360</u>
Consultants and foster parents	78,140	440	356	12,253	91,189
Accounting and audit	-	-	-	16,790	16,790
Staff training	43,360	2,145	1,858	4,069	51,432
Mileage reimbursement	23,736	10,119	2,410	5,375	41,640
Vehicle lease	31,233	-	-	-	31,233
Vehicle repairs and supplies	10,228	-	3,154	389	13,771
Telephone	15,314	817	692	16,024	32,847
Postage	14	-	-	2,486	2,500
Rent / lease	45,575	-	-	28,800	74,375
Utilities	29,533	-	43	5,657	35,233
Building remodel and maintenance	25,099	-	145	6,909	32,153
Equipment and furniture purchase	5,291	-	-	(43)	5,248
Equipment and furniture repair	3,335	-	-	125	3,460
Medical equipment and supplies	(7)	-	-	-	(7)
Program services	3,085	15	16	4,133	7,249
Activity costs	5,258	82	5	482	5,827
Food	44,399	10	47	375	44,831
Office supplies	6,105	250	-	15,861	22,216
Other supplies	5,862	186	54	5,572	11,674
Conference per diem	311	-	-	7,658	7,969
Books and subscriptions	200	258	-	6,049	6,507
Insurance expense	45,176	1,995	5,573	3,589	56,333
Licenses and permits	4,910	250	219	851	6,230
Miscellaneous expense	334	-	-	251	585
Interest	37,414	-	-	-	37,414
Depreciation	26,698	-	718	4,149	31,565
	<u>\$ 1,953,703</u>	<u>\$ 173,256</u>	<u>\$ 92,382</u>	<u>\$ 352,283</u>	<u>\$ 2,571,624</u>
Total expenses					

See accompanying notes and accountants' report.

AVATAR, INC.

STATEMENT OF FUNCTIONAL EXPENSES

Year ended June 30, 2004

	Group Homes	Family Support	Supported Employment	Management and General	Company Total
Salaries and related expenses:					
Salaries	\$ 1,292,291	\$ 108,556	\$ 66,190	\$ 338,437	\$ 1,805,474
Employee fringe benefits	-	-	-	37,867	37,867
Payroll taxes	101,232	8,855	5,273	33,053	148,413
	<u>1,393,523</u>	<u>117,411</u>	<u>71,463</u>	<u>409,357</u>	<u>1,991,754</u>
Consultants and foster parents	12,341	91,917	-	6,741	110,999
Accounting and audit	2,731	-	-	4,742	7,473
Staff training	33,127	3,942	406	4,713	42,189
Mileage reimbursement	20,923	8,597	2,396	1,939	33,855
Vehicle lease	30,504	-	-	-	30,504
Vehicle repairs and supplies	9,596	-	(91)	-	9,505
Telephone	15,059	1,722	282	13,548	30,611
Postage	89	27	-	2,635	2,751
Rent / lease	37,800	-	-	29,501	67,301
Utilities	28,989	-	-	5,271	34,260
Building remodel and maintenance	25,062	-	37	5,946	31,045
Equipment and furniture purchase	795	-	-	635	1,430
Equipment and furniture repair	2,672	-	-	1,043	3,715
Medical equipment and supplies	-	-	-	-	-
Program services	7,266	946	15	(3,011)	5,216
Activity costs	5,562	130	21	379	6,092
Food	38,378	-	31	(3,412)	34,997
Office supplies	5,784	393	235	10,566	16,978
Other supplies	10,455	445	662	1,887	13,449
Conference per diem	1,836	229	-	11,003	13,068
Books and subscriptions	210	-	-	6,288	6,498
Insurance expense	-	-	-	69,869	69,869
Licenses and permits	2,958	250	-	120	3,328
Miscellaneous expense	1,762	-	191	1,137	3,090
Interest	47,109	-	-	41	47,150
Depreciation	<u>21,507</u>	<u>-</u>	<u>117</u>	<u>3,026</u>	<u>24,650</u>
Total expenses	<u>\$ 1,756,038</u>	<u>\$ 226,009</u>	<u>\$ 75,765</u>	<u>\$ 583,964</u>	<u>\$ 2,641,777</u>

See accompanying notes and accountants' report.

AVATAR, INC.
STATEMENTS OF CASH FLOWS
Years Ended June 30, 2005 and 2004

	<u>2005</u>	<u>2004</u>
CASH FLOWS FROM OPERATING ACTIVITIES		
Increase (decrease) in net assets	\$ 13,923	\$ (90,052)
Adjustments to reconcile change in net assets to net cash provided by operating activities :		
Depreciation and amortization	57,447	25,764
Changes in operating assets and liabilities :		
Accounts receivable	40,302	36,917
Prepaid expense and deposits	(10,838)	(8,432)
Assets limited as to use	1,804	43
Accounts payable	(512)	15,026
Accrued expenses	<u>23,062</u>	<u>(2,773)</u>
NET CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES	19,816	(23,507)
CASH FLOWS FROM INVESTING ACTIVITIES		
Loans payable	20,631	-
Purchase of property and equipment	<u>(51,797)</u>	<u>(3,688)</u>
NET CASH USED IN INVESTING ACTIVITIES	(31,166)	(3,688)
CASH FLOWS FROM FINANCING ACTIVITIES		
Principal payments of long-term debt	<u>(25,764)</u>	<u>(24,639)</u>
NET CASH USED IN FINANCING ACTIVITIES	<u>(25,764)</u>	<u>(24,639)</u>
NET DECREASE IN CASH AND CASH EQUIVALENTS	(37,114)	(51,834)
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	<u>31,858</u>	<u>83,692</u>
CASH AND CASH EQUIVALENTS AT END OF YEAR	<u><u>\$ (5,255)</u></u>	<u><u>\$ 31,858</u></u>

See accompanying notes and accountants' report

AVATAR, INC.
NOTES TO FINANCIAL STATEMENTS
June 30, 2005

1. NATURE OF ACTIVITIES AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of Activities

Avatar, Inc. (the Organization) is a non-profit corporation organized under the Utah Nonprofit Corporation and Cooperative Association Act. The principal objective and purpose for which the Organization was formed, as stated in its articles of incorporation, is to provide quality habilitative and rehabilitative services to persons with handicapping conditions and disabilities in the State of Utah.

Basis of Accounting

The accounts of the Organization are maintained and the financial statements are prepared on the accrual basis of accounting. Accordingly, revenues and gains are recognized when earned, and expenses and losses are recognized when incurred.

Basis of Presentation

In accordance with SFAS No. 117, Financial Statements of Not-for-Profit Organizations, the Organization reports information regarding its financial position and activities according to three classes of net assets: unrestricted net assets, temporarily restricted net assets, and permanently restricted net assets.

Use of Estimates

The financial statements include estimates and assumptions made by management that affect the carrying amounts of assets and liabilities, the disclosure of contingent assets and liabilities, and the reported amounts of revenues and expenses. Actual results could differ from those estimates.

Property and Equipment

Acquisitions of property and equipment in excess of \$1,000 are capitalized. Property and equipment are carried at cost or, if donated, at the approximate fair value at the date of donation. Depreciation is computed on the straight-line method over the estimated useful lives of the assets (3 to 30 years).

AVATAR, INC.
NOTES TO FINANCIAL STATEMENTS
June 30, 2005

1. NATURE OF ACTIVITIES AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Revenue Recognition

Revenue and expenses are recorded on the accrual basis. Contributions received are recorded as unrestricted, temporarily restricted, or permanently restricted support, depending on the existence and/or nature of any donor restrictions.

All other donor-restricted support is reported as an increase in temporarily or permanently restricted net assets, depending on the nature of the restriction. When a restriction expires (that is, when a stipulated time restriction ends or purpose restriction is accomplished), temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statement of activities as net assets released from restrictions.

Concentration of Revenue Sources

Government contracts represent approximately 95% and 94% of the Organization's source of revenues in fiscal 2005 and 2004, respectively.

Income Taxes

The Organization is exempt from federal income tax under Section 501(c)(3) of the Internal Revenue Code. However, income from certain activities not directly related to the Organization's tax-exempt purpose is subject to taxation as unrelated business income.

Cash and Cash Equivalents

Cash and cash equivalents includes all monies in banks and highly liquid investments with maturity dates of less than three months. The carrying value of cash and cash equivalents approximates fair value because of the short maturities of those financial instruments.

Assets Limited as to Use

Assets deposited with a trustee under terms of the note indenture (note 2) are classified as assets limited as to use.

AVATAR, INC.
NOTES TO FINANCIAL STATEMENTS
June 30, 2005

1. NATURE OF ACTIVITIES AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Unamortized Bond Costs

Costs incurred in connection with the issuance of the Clearfield City, UT/UARF, Series 1997 Tax Exempt Bonds are amortized over the term of the bonds using the effective-interest method.

Functional Allocation of Expenses

The costs of providing the various programs and activities have been summarized on a functional basis in the statement of activities. Accordingly, certain costs have been allocated among the programs and supporting services benefited.

2. ASSETS LIMITED AS TO USE

The assets limited as to use are composed of the following:

	<u>2005</u>	<u>2004</u>
CURRENT:		
Cash in money market accounts, designated for the bond sinking fund	<u>\$ 9,854</u>	<u>\$ 11,658</u>
NON-CURRENT:		
Debt service reserve fund	<u>\$ 25,000</u>	<u>\$ 25,000</u>

AVATAR, INC.
NOTES TO FINANCIAL STATEMENTS
June 30, 2005

3. PROPERTY AND EQUIPMENT

Property and equipment at June 30 consisted of the following:

	<u>2005</u>	<u>2004</u>
Land	\$ 162,000	\$ 161,000
Buildings	587,222	586,003
Furniture and equipment	159,842	126,895
Vehicles	<u>27,178</u>	<u>10,547</u>
	936,242	884,445
Accumulated depreciation	<u>(228,567)</u>	<u>(197,002)</u>
	<u>\$ 707,675</u>	<u>\$ 687,443</u>

4. INTANGIBLE ASSETS

Intangible assets at June 30 consisted of the following:

	<u>2005</u>	<u>2004</u>
Prepaid loan fees	\$ 8,145	\$ 8,145
Bond issuance fees	<u>14,265</u>	<u>14,265</u>
	22,410	22,410
Accumulated amortization	<u>(5,638)</u>	<u>(4,524)</u>
	<u>\$ 16,772</u>	<u>\$ 17,886</u>

The prepaid loan fees and bond issuance costs are amortized over 15 years.

AVATAR, INC.
NOTES TO FINANCIAL STATEMENTS
June 30, 2005

5. NOTES PAYABLE

	<u>2005</u>	<u>2004</u>
Clearfield City, UT/UARF Mortgage Revenue Bonds, with interest at 7.70% due in increasing annual installments of \$5,000 in 1998 to \$25,000 in 2022, with interest due semi-annually, secured by real estate and the net rental revenue	\$ 250,000	\$ 255,000
Washington Mutual, with interest at 5.625% and monthly payments of \$922.58, maturing August, 2017, collateralized by real estate	97,897	102,905
Washington Mutual, with interest at 5.625% and monthly payments of \$996.72, maturing August, 2017, collateralized by real estate	104,839	110,773
Washington Mutual, with interest at 5.625% and monthly payments of \$762.78, maturing August, 2017, collateralized by real estate	81,280	85,724
Washington Mutual, with interest at 5.625% and monthly payments of \$787.49, maturing August, 2017, collateralized by real estate	<u>83,125</u>	<u>88,502</u>
Total	617,141	642,904
Less current maturities of long-term debt	<u>(26,385)</u>	<u>(25,217)</u>
Net long-term debt	<u>\$ 590,756</u>	<u>\$ 617,687</u>

AVATAR, INC.
NOTES TO FINANCIAL STATEMENTS
June 30, 2005

5. NOTES PAYABLE (Continued)

Notes payable mature as follows:

<u>Year Ended June 30</u>	<u>Amount</u>
2006	\$ 26,385
2007	27,617
2008	28,925
2009	30,306
2010	31,766
Thereafter	<u>472,929</u>
	<u>\$ 617,928</u>

Interest accrued on notes and mortgages as of June 30, 2005 and 2004 was \$3,435 and \$3,514, respectively.

6. COMMITMENTS

Operating Leases

Avatar, Inc. is obligated under operating leases for group homes, office space and certain equipment. Such leases are summarized below:

<u>Facility</u>	<u>Expiration Date</u>	<u>Annual Costs</u>
South Ogden Program	Month-to-month	\$ 10,800
American Fork Program	Month-to-month	14,400
Clinton Group Home	Month-to-month	13,200
Utah Office	April 2007	22,140
Vehicles and Equipment	Various to 6/2010	37,748

Operating lease commitments for the next five years are as follows:

<u>Year ended June 30</u>	<u>Amount</u>
2006	\$ 59,281
2007	28,919
2008	10,469
2009	10,469
2010	10,469
Thereafter	-
	<u>\$ 119,607</u>

AVATAR, INC.
NOTES TO FINANCIAL STATEMENTS
June 30, 2005

6. COMMITMENTS (Continued)

Rental expenses under operating leases for the years ended June 30, 2005 and 2004 were \$74,375 and \$67,301, respectively.

Insurance and maintenance expenses are generally obligations of the Organization and accordingly are not included as part of the rental payments.

7. SUPPLEMENTAL CASH FLOW INFORMATION

Cash paid for interest totaled \$33,504 and \$46,575 for the years ended June 30, 2005 and 2004, respectively.

8. OFFICER LOAN PAYABLE

During the year ended June 30, 2005, the Organization borrowed \$20,631 from the executive director to purchase a vehicle and equipment. The loan has an interest rate of 5.75 percent with no set equipment terms. There was accrued interest of \$475 on the loan as of June 30, 2005.



CARVER HOVEY & FLOREK, LLC

CERTIFIED PUBLIC ACCOUNTANTS

STEVEN L. CARVER, CPA
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BRENT R. FLOREK, CPA

REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

To the Board of Trustees
Avatar, Inc.

We have audited the financial statements of Avatar, Inc. (a non-profit organization) as of and for the year ended June 30, 2005, and have issued our report thereon dated October 14, 2005. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether Avatar, Inc.'s financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Avatar, Inc.'s internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

This report is intended for the information and use of the management of Avatar, Inc. and state and federal awarding agencies, and is not intended to be and should not be used by anyone other than these specified parties.

Carver Hovey & Florek, LLC

October 14, 2005



CARVER HOVEY & FLOREK, LLC

CERTIFIED PUBLIC ACCOUNTANTS

STEVEN L. CARVER, CPA
KATHLEEN L. HOVEY, CPA
BRENT R. FLOREK, CPA

REPORT ON STATE LEGAL COMPLIANCE

To the Board of Trustees
Avatar, Inc.

We have audited the financial statements of Avatar, Inc. (a non-profit organization) as of and for the year ended June 30, 2005, and have issued our report thereon dated October 14, 2005. As part of our audit, we have audited Avatar, Inc.'s compliance with the requirements governing types of services allowed or unallowed; eligibility; matching, level of effort, or earmarking; reporting; special tests and provisions applicable to its major State assistance program as required by the State of Utah Legal Compliance Audit Guide for the year ended June 30, 2005. Avatar, Inc. received the following major State assistance program from the state of Utah:

RESIDENTIAL

The management of Avatar, Inc. is responsible for its compliance with the compliance requirements identified above. Our responsibility is to express an opinion on compliance with those requirements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether material noncompliance with the requirements referred to above occurred. An audit includes examining, on a test basis, evidence about Avatar, Inc.'s compliance with those requirements. We believe that our audit provides a reasonable basis for our opinion.

The results of our audit procedures disclosed no instances of noncompliance with the requirements referred to above.

In our opinion, Avatar, Inc. complied, in all material respects, with the requirements governing types of services allowed or unallowed; eligibility; matching, level of effort, or earmarking; reporting; and special tests and provisions that are applicable to its major State assistance program for the year ended June 30, 2005.

Carver Hovey & Florek, LLC

October 14, 2005